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Supreme Court of the United States

OCTOBER TERM, 1941.

No. 896.

FAITOUTE IRON & STEEL COMPANY, THE HOWARD SAVINGS INSTITUTION, FLORENCE W. FAITOUTE, *et als.*,

Appellants,

vs.

CITY OF ASBURY PARK, a Municipal Corporation of the State of New Jersey,

Appellee.

On Appeal from the Court of Errors and Appeals of New Jersey.

BRIEF OF APPELLEE.

WARD KREMER,
Attorney of Appellee.

MacCrellish & Quigley Co., Printers, Trenton, New Jersey

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Appellants,

vs.

CITY OF ASBURY PARK, a Municipal Corporation of the State of New Jersey,

Appellee.

ON APPEAL FROM THE COURT OF ERRORS AND APPEALS OF NEW JERSEY.

BRIEF OF APPELLEE.

I.

The Opinions of the Courts Below.

The opinion of the Supreme Court of New Jersey is reported in 19 N. J. Misc. 322, and appears in the Record at page 65.

The opinion of the Court of Errors and Appeals of New Jersey is reported in 127 N. J. L. 239, and appears in the Record at page 70.

II.

The Grounds on Which the Jurisdiction of This Court Is Invoked by the Appellants.

The appellants invoke the jurisdiction of this Court on two grounds:

1. It is contended by the appellants that the provisions of Article 7 of Chapter 27 of Title 52 of the Revised Statutes of New Jersey, comprising Sections 52:27-34 to 52:27-39 are unconstitutional in that they impair the obligation of contracts in violation of Article I, Section 10 of the Constitution of the United States (R., p. 77).

2. It is contended by the appellants that the provisions of Article 7 of Chapter 27 of Title 52 of the Revised Statutes of New Jersey, comprising Sections 52:27-34 to 52:27-39, are unconstitutional, in that they deprive appellants of property without due process of law, deny appellants the equal protection of the laws, and abridge the privileges and immunities of citizens of the United States in violation of the Fourteenth Amendment to the Constitution of the United States (R., p. 78).

III.

Statement of Case.

The New Jersey Court of Errors and Appeals sustained the validity of the New Jersey statute, Article 7 of Chapter 27 of Title 52 of the Revised Statutes, enacted June 27, 1933. This statute is, in reality, a supplement to the Municipal Finance Commission Law enacted in New Jersey April 28, 1931, and constituting Chapter 27 of Title 52 of the Revised Statutes of New Jersey, comprising Sections 52:27-1 to 52:27-39.*

* The applicable sections of Chapter 27 of Title 52 of the Revised Statutes are printed as an Appendix to this Brief.

In 1931 the State of New Jersey, by appropriate legislation, created a Municipal Finance Commission consisting of the Attorney-General, the State Tax Commissioner and the State Auditor (R. S. 52:27–1). The purpose of the legislation was, manifestly, to meet the situation resultant from the economic depression and to set up a state agency which would protect taxpayers, property owners and security holders alike. In fact, the New Jersey Legislature declared its intention in the act itself, which contains the following provision:

> "Remedial law to meet public emergency; liberal construction
>
> "It is declared that this chapter is intended by the legislature to meet the public emergency arising from a default in the payment of municipal and school district obligations and the resulting impairment of public credit, requiring intervention by the state to provide for the payment of existing obligations in such a way as to cause the least embarrassment to property owners as taxpayers, and that this chapter is remedial in nature and the powers hereby granted shall be liberally construed." (R. S. 52:27–65.)

The act provides that, upon the filing of a petition by any bondholder reciting that the municipality had defaulted for over sixty days in the payment of principal or interest of any of its outstanding obligations, the State Supreme Court Justice to whom the petition was presented might make a summary investigation of the matter (R. S. 52:27–2).

This section further provides that if the justice be satisfied that the municipality is in default, he may make an order to that effect, and upon the filing of the same, the Municipal Finance Commission "shall have and exercise

with respect to such municipality the powers and duties prescribed by this chapter."

The jurisdiction of the Court and the commission may also be invoked by the municipality itself, upon its filing with a justice of the Supreme Court a resolution reciting that "due to unusual conditions the municipality is not in a position to meet its obligations when due, in spite of the endeavors of its officers, and petitioning that the commission shall function in the municipality." (R. S. 52:27–3)

Upon the assumption of its duties by the commission, all governmental powers of the elected governing body are henceforth subject to the approval and supervision of the commission. No moneys may be disbursed unless the warrants or checks are countersigned by the auditor appointed by the commission (R. S. 52:27–9).

Upon the failure of the municipal officials to carry out any direction of the commission, the commission may perform directly, or cause to be performed by its agents, in the name of the municipality, any act so directed by the commission, including the power to execute, sell, issue and deliver bonds or notes (R. S. 52:27–13).

The auditor hereinabove referred to, who is, in reality, the representative of the commission in the municipality, is given power "to review all contracts prior to their execution and authorization by the governing body; to recommend the tentative annual budget to the governing body thereof and to the commission; to make recommendations concerning all capital improvements; to investigate the affairs of any department." (R. S. 52:27–13.1.)

The commission is given power to require the appointment of special tax collectors (R. S. 52:27–13.3).

Its powers include the power to provide a budget for the municipality and to direct the Commissioner of Local Government to certify to the said governing body tax levies

for debt service in any certain amounts fixed by the commission. *City of Asbury Park* v. *Darby*, 15 N. J. Misc. 311.

The legislation further empowered the commission to certify to the governing body of the municipality in which it is functioning "resolutions providing for the funding or refunding of notes or bonds or other indebtedness of the municipality, and the interest thereon, which the commission shall have found after public hearing to be outstanding and unpaid and to be due or to become due." (R. S. 52:27–14.)

Resolutions of the commission for the issuance of notes or bonds must "on direction of the commission, be adopted by the proper officials of such municipality in the form certified by the commission." (R. S. 52:27–16.)

Further provisions are made for the publication of the resolutions adopted (R. S. 52:27–18); for the terms and form of the notes or bonds (R. S. 52:27–19); and for the public sale of the securities (R. S. 52:27–20).

It is not necessary for present purposes to recite these provisions in detail. However, it is appropriate to refer specifically to Subdivision b. of Section 52:27–20, which reads as follows:

> "b. With the approval in writing of the commission, any notes or bonds or part thereof may be exchanged for any notes or bonds, including interest thereon, of the municipality issued under this or any other law. The rate of interest borne by any such notes or bonds may be higher or lower than the rate of interest borne by the notes or bonds surrendered."

The legislation was obviously designed for the protection of bondholders and taxpayers alike. The act vested the Municipal Finance Commission with the power, to all intents and purposes, to impound the funds of the munici-

pality. Clothed with the power to provide the municipal budget, the commission could direct the amount of money which must be assessed and levied against property in the community. No moneys could be disbursed except upon the authority of the commission or its accredited representative. An effective brake upon municipal expenditures was thus provided, as a result of which funds became available for the payment of bonds and other outstanding obligations.

The Legislature went on to provide that while the commission was functioning in any municipality, no judgment or execution should be enforced against the municipality for the recovery of the amount due on any municipal bonds unless ordered by a Supreme Court Justice, and that the enforcement of any such judgment should be stayed unless otherwise specially ordered (R. S. 52:27–32.1).

The Legislature, having set up an agency to protect security holders in distressed municipalities and to provide an orderly method for the assembling of the reserves of the municipalities and the payment of the security holders, apparently intended that they should all be treated on a parity, and that while the commission's functions were in progress, no single bondholder should secure an advantage over others in the same class.

The legislation above referred to was entitled "An Act Concerning Municipal Finances" (Laws of New Jersey 1931, Chap. 340), and became Chapter 27 of Title 52 of the Revised Statutes of New Jersey (R. S. 52:27–1 *et seq.*).

On June 27, 1933, the Legislature enacted Chapter 331 of the Laws of 1933 entitled "An Act to Supplement an Act entitled 'An Act Concerning Municipal Finances,' approved April 28, One Thousand Nine Hundred and Thirty-one, constituting Chapter 340 of the Laws of One Thousand Nine Hundred and Thirty-one," and this act is now Article 7 of Chapter 27 of Title 52 of the Revised Statutes of New Jersey, comprising Sections 52:27–34 to 52:27–39, inclusive.

It is this supplement which is the subject of appellants' attack, but it will be observed that while it was enacted subsequent to the original legislation, it was enacted as and became an integral part thereof. In construing the enactment of 1933, it must be read in connection with the statute of which it became a part.

The supplement provided that, in a municipality in which the Municipal Finance Commission was functioning, creditors might file a petition with the Supreme Court Justice for the composition of the claims of all creditors—that the justice might take jurisdiction of the subject matter of the petition, and that the commission and all creditors must be given notice thereof (R. S. 52:27–34).

It was required that the petition should allege that the proposed plan or composition "is substantially measured by the capacity of the municipality to pay, *is in the interests of all the creditors affected thereby,* and is not detrimental to other creditors of the municipality." (R. S. 52:27–35.)*

The act then provided that if, after hearing on the plan proposed, it was approved in writing by creditors representing eighty-five per cent in amount of the indebtedness affected thereby and by the municipality and the commission, the Court might approve such plan if the justice determined certain facts to exist. These findings are "(1) that the municipality is unable to pay in full according to their terms the claims proposed to be adjusted or composed, and perform its public functions and preserve the value of property subject to taxation, (2) that the adjustment or composition is substantially measured by the capacity of the municipality to pay, (3) that it is in the interest of all the creditors affected thereby, and (4) that it is not detrimental to other creditors of the municipality." (R. S. 52:27–36.)

* All italics ours unless otherwise noted.

A plan of adjustment so authorized and approved is binding upon *all creditors included in the plan, whether or not they appear in the proceeding.* (R. S. 52:27–37.)

The act further provides that after approval of a plan no creditor whose claim is included in the adjustment shall be authorized to bring any action for the enforcement of his claim, *except with the permission of the Supreme Court,* and then only to recover and enforce the rights given him by the adjustment or composition (R. S. 52:27–38).

The final pertinent provision in the act is that no plan of adjustment may be approved by the commission which provides for the reduction in the principal amount of any outstanding bonds of the municipality. (R. S. 52:27–39.)

Under this legislation, the City of Asbury Park, which had been placed under the control of the Municipal Finance Commission on March 7, 1935, accomplished a refunding of its outstanding bonded indebtedness in the amount of $10,750,000. The facts concerning this refunding are referred to in some detail in the statement of case in appellants' brief, and they are not reiterated here. It is important to state, however, that the bonds of the appellants were included in the city's refunding plan. This appears in the affidavit of Walter Haight, the Auditor and Comptroller of the City (R., p. 61), and it has never been denied by the appellants (Affidavit of Moses W. Faitoute, R., p. 63).

It is equally true that when appellants instituted their suit on their bonds in the New Jersey Supreme Court, they did not secure the permission of the Supreme Court in accordance with R. S. 52:27–38 (Opinion of New Jersey Supreme Court, R., pp. 65, 67). It was on account of the failure of the appellants to secure or to apply for this permission that their action was dismissed in the tribunal in which it was originally instituted.

The affidavit of the City Manager, Milford G. Farley (R., p. 9) sets forth in detail the proceedings undertaken by the city for the refunding of its indebtedness, and recites the transactions which resulted in the consummation of the refunding plan and the placing of the same in operation. It is not contradicted by the appellants and it leaves no doubt that the provisions of the statute were complied with completely.

The New Jersey Supreme Court struck the complaint of the appellants for the reason that they had not applied for nor secured permission of the Court to bring the suit (R., p. 65). The Court of Errors and Appeals of New Jersey affirmed the Supreme Court and held that the legislation herein outlined is constitutional.

IV.

ARGUMENT.

Summary of Argument.

Point I. The Court of Errors and Appeals of New Jersey did not err in affirming the judgment of the Supreme Court of New Jersey dismissing the appellants' complaint, since Article 7 of Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937) and Chapter 27 of Title 52 of the Revised Statutes of New Jersey are constitutional enactments and do not impair the obligation of contracts.

Point II. The statute is a lawful exercise of the police power, whether considered as an emergency measure or as permanent legislation.

Point III. Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937) and Article 7 of Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937) do not deprive appellants of property without due process of law and do not deny to appellants the equal protection of

the laws, nor abridge the privileges and immunities of citizens of the United States in violation of the Fourteenth Amendment to the Constitution of the United States.

Point IV. The enactment by Congress of the Federal Municipal Bankruptcy Act August 16, 1937, had no effect whatever upon the validity of the refunding proceeding consummated by the City of Asbury Park pursuant to the New Jersey statute.

POINT I.

The statute, Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937) and Article 7 of Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937), is constitutional and does not impair the obligation of contracts.

The Court of Errors and Appeals of New Jersey passed upon the constitutionality of the so-called Municipal Finance Commission Law (Chapter 27 of Title 52 of the Revised Statutes of New Jersey) in the case of *Hourigan* v. *North Bergen Township*, 113 N. J. L. 143 (1934).

In that case the appellants challenged the constitutionality of the statute on the same ground upon which it is challenged here, contending that the legislation was repugnant to Article I, Section 10 of the Federal Constitution. The New Jersey Court took notice of the fact that it was emergency legislation and recited the legislative declaration of the emergency in its opinion. Mr. Justice Heher, speaking for the Court, said:

> "The finding of the legislature that an emergency exists has a factual basis of which we take judicial notice. The legislation is addressed to a legitimate end, and the measures taken are reasonable and appropriate to that end. *Home Building and Loan Association* v. *Blaisdell*, 290 U. S. 398."

Referring to the legislative purpose, Mr. Justice Heher said:

"The act confers upon the finance commission, in respect of the municipality's financial affairs, powers somewhat akin to those exercised by receivers of insolvent corporations. It was designed to give support to the tottering municipalities, and to prevent complete collapse and total paralysis of function. It embodies wise and useful provisions tending to restrain and check the reckless levy of taxes, and to promote economy and the orderly conduct of the municipality's affairs. Its primary purpose is to keep intact the corporate structure, and to continue municipal function until rehabilitation can be affected.

"*This is, of necessity, a proper legislative function, and the rights of creditors, in such a situation, are secondary.* It is a proper exercise of the police power. It is a well established doctrine that the interdiction of statutes impairing the obligation of contracts does not prevent the state from exercising such powers as are vested in it for the promotion of the common weal, or are necessary for the general good of the public, though contracts entered into between individuals may thereby be affected. This power, which in its various ramifications is known as the police power, is an exercise of the sovereign right of the government to protect the lives, health, morals, comfort and general welfare of the people; and is paramount to any rights under contracts between individuals. While this power is subject to limitations in certain cases, there is wide discretion on the part of the legislature in determining what is and what is not necessary—a discretion which courts ordinarily will not interfere with. *Manigault* v. *Springs*, 199 U. S. 473; 26 Sup. Ct. 127; 50 L. Ed. 274; *Union Dry Goods Co.* v. *Georgia Public Service*

> *Corp.*, 248 U. S. 372. The proper exercise of the police power is the highest duty of government. The state may, in some cases, forego the right of taxation, but it can never relieve itself of the duty of providing for the safety of its citizens. This duty, and consequent power, override all statute or contract exemptions. The state cannot free any person or corporation from subjection to this power. All personal as well as property rights must be held subject to the police power of the state."

The Court quoted and followed the decision of this Court in *Home Building and Loan Association* v. *Blaisdell, supra*; and discussed the fact that the Municipal Finance Commission legislation fixed no limit to the efficacy of the legislation as distinguished from the statute under scrutiny in the *Blaisdell* case. Mr. Justice Heher proceeded to observe:

> "But it is not requisite that the operation of the law be limited to a definite term. It is the actual existence of the emergency solely, and not the limitation of the law's operation to a prescribed period, that gives validity of this exercise of the reserve element of sovereignty called the police power."

In *Home Building & Loan Association* v. *Blaisdell*, 290 U. S. 398, attack was made upon the Minnesota statute known as the Minnesota Mortgage Moratorium Law as being repugnant to the contract clause (Art. I, Section 10), and the due process and equal protection clauses of the Fourteenth Amendment of the Federal Constitution. The act provided that during the emergency which was declared to exist, relief might be had through authorized judicial proceedings with respect to foreclosure of mortgages and execution sales thereunder. The period of re-

demption could be extended by the Court, and the mortgagor was permitted to apply all or a reasonable part of the income from the property toward the payment of taxes, insurance, interest and the mortgage indebtedness. All of these provisions were in contravention of the contractual relations established between mortgagor and mortgagee at the time the legislation was enacted. Mr. Chief Justice Hughes delivered the opinion of this Court, and said:

> "The state court upheld the statute as an emergency measure. Although conceding that the obligations of the mortgage contract were impaired, the court decided that what it thus described as an impairment was, notwithstanding the contract clause of the Federal Constitution, within the police power of the State as that power was called into exercise by the public economic emergency which the legislature had found to exist. * * *
>
> "This Court has said that '*the laws which subsist at the time and place of the making of a contract, and where it is to be performed, enter into and form a part of it, as if they were expressly referred to or incorporated in its terms.*' This principle embraces alike those which affect its validity, construction, discharge and enforcement. * * *
>
> "Not only is the constitutional provision qualified by the measure of control which the State retains over remedial processes, but the State also continues to possess authority to safeguard the vital interests of its people. It does not matter that legislation appropriate to that end 'has the result of modifying or abrogating contracts already in effect.' *Stephenson* v. *Binford*, 287 U. S. 251, 276, 77 L. ed. 288, 301, 53 S. Ct. 181, 87 A. L. R. 721. Not only are existing laws read into contracts in order to fix obligations as between the parties, but the reservation of essential attributes of sovereign power is also read

into contracts as a postulate of the legal order. The policy of protecting contracts against impairment presupposes the maintenance of a government by virtue of which contractual relations are worth while—a government which retains adequate authority to secure the peace and good order of society. This principle of harmonizing the constitutional prohibition with the necessary residuum of state power has had progressive recognition in the decisions of this Court."

The learned Chief Justice discussed the contract clause of the Federal Constitution and its history at some length, and observed:

> "To ascertain the scope of the constitutional prohibition, we examined the course of judicial decisions in its application. These put it beyond question that the prohibition is not an absolute one and is not to be read with literal exactness like a mathematical formula. • • •
>
> "The economic interests of the State may justify the exercise of its continuing and dominant protective power notwithstanding interference with contracts."

The Chief Justice quoted *Manigault v. Springs*, 199 U. S. 473, in which the principle had been stated as follows:

> "The Court said: 'It is the settled law of this court that the interdiction of statutes impairing the obligation of contracts does not prevent the State from exercising such powers as are vested in it for the promotion of the common weal, or are necessary for the general good of the public, though contracts previously entered into between individuals may thereby be affected.'"

At another point in the opinion, the Chief Justice said:

> "Whatever doubt there may have been that the protective power of the State, its police power, may be exercised—without violating the true intent of the provision of the Federal Constitution—in directly preventing the immediate and literal enforcement of contractual obligations by a temporary and conditional restraint, where vital public interests would otherwise suffer, was removed by our decisions relating to the enforcement of provisions of leases during a period of scarcity of housing. *Block* v. *Hirsh*, 256 U. S. 135, 65 L. ed. 865, 41 S. Ct. 458; 16 A. L. R. 165; *Marcus Brown Holding Co.* v. *Feldman*, 256 U. S. 170, 65 L. ed. 877, 41 S. Ct. 465; *Edgar A. Levy Leasing Co.* v. *Siegel*, 258 U. S. 242, 66 L. ed. 595, 42 S. Ct. 289."

In *Block* v. *Hirsh*, 256 U. S. 135, emergency legislation growing out of the housing shortage and permitting tenants to hold over after the expiration of the lease, subject to regulation by a commission appointed in the act, was under attack. Mr. Justice Holmes, speaking for the Court, said:

> "The general proposition to be maintained is that circumstances have clothed the letting of buildings in the District of Columbia with a public interest so great as to justify regulation by law. Plainly, circumstances may so change in time or so differ in space as to clothe with such an interest what at other times or in other places would be a matter of purely private concern."

After referring to a line of decisions in support of the principle enunciated, the Justice said:

> "They dispel the notion that what in its immediate aspect may be only a private transaction may not be raised by its class or character to a public affair."

The question of the legislative power to enact a law necessary for reasons of economic safety and for the prevention of economic collapse of the State in the face of the provisions of the contract clause of the Federal Constitution, was put at rest in the so-called Gold Clause cases (*Norman* v. *Baltimore & Ohio Railroad Company*, 294 U. S. 240; *Nortz* v. *The United States*, 294 U. S. 317; *Perry* v. *The United States*, 294 U. S. 330).

In *Norman* v. *Baltimore & Ohio Railroad Company*, *supra*, this Court, speaking through Mr. Chief Justice Hughes, passed upon the validity of the joint resolution of Congress of June 5, 1933 with respect to the "Gold Clauses" of private contracts for the payment of money. The resolution relieved the government from the duty to pay in gold dollars of standard weight and fineness of 25 8/10 grains of gold nine-tenths fine, and substituted gold dollars to consist of 15 5/21 grains of gold nine-tenths fine. There can be no question that the value of the thing to be received by the obligee was thus decreased. The Court, speaking through the learned Chief Justice, passed directly upon "the power of Congress to invalidate the provisions of existing contracts which interfere with the exercise of its constitutional authority." The Chief Justice said:

> "Contracts, however express, cannot fetter the constitutional authority of the Congress. Contracts may create rights of property, but when contracts deal with a subject matter which lies within the control of the Congress, *they have a congential infirmity.* Parties cannot remove their transactions from the reach of dominant constitutional power by making contracts about them. See *Hudson Water Co.* v. *McCarter*, 209 U. S. 349, 357, 52 L. ed. 828, 832, 28 S. Ct. 529, 14 Ann. Cas. 560."

Applying the same principle as it was adjudicated upon in the legal tender cases, the Court said:

> "Quoting the statement of the general principle in the legal tender cases, the Court decided that the agreement must necessarily be regarded as having been made subject to the possibility that, at some future time, the Congress 'might so exert its whole constitutional power in regulating interstate commerce as to render that agreement unenforceable or to impair its value.' The Court considered it inconceivable that the exercise of such power 'may be hampered or restricted to any extent by contracts previously made between individuals or corporations.' 'The framers of the Constitution never intended any such state of things to exist.' "

The same reasoning was applied at a later point in the opinion, as follows:

> "To subordinate the exercise of the Federal authority to the continuing operation of previous contracts would be to place to this extent the regulation of interstate commerce in the hands of private individuals and to withdraw from the control of the Congress so much of the field as they might choose by 'prophetic discernment' to bring within the range of their agreements. The Constitution recognizes no such limitation."

In *Nortz* v. *The United States, supra,* the plaintiff, the holder of gold certificates, complained that he was required to exchange them for currency not redeemable in gold. Enunciating the same principles applied in *Norman* v. *Baltimore & Ohio Railroad Company, supra,* the Court held that the security holder was not deprived of his property "although at the time of being required to surrender

the certificates the market price of the gold represented by the certificates was in excess of the currency received."

In other words, even the admitted fact that the money received by the security holder was of lesser value than the market price at the time of the gold represented by the security, did not render the transaction nor the legislation authorizing it unconstitutional, in view of the paramount legislative power in the circumstances.

No distinction can be drawn between the monetary loss sustained by the security holders in *Nortz* v. *The United States, supra,* and *Perry* v. *The United States, supra,* in being compelled to accept securities of an alleged lesser value than those they previously held, and the loss claimed to have been sustained by appellants in the instant case, in being compelled to accept a bond bearing a lower rate of interest than the obligation for which it is substituted. Both transactions find their basis in the same legislative power.

In *Norman* v. *Baltimore & Ohio Railroad Company, supra,* the Court referred, with approval, to *Hudson County Water Company* v. *McCarter,* 209 U. S. 349, in which this Court passed upon the question whether legislation enacted in the State of New Jersey under which the diversion of water beyond the State was forbidden, impaired the obligation of a contract to divert the waters of the Passaic River into another State. Discussing the applicability of the contract clause of the Federal Constitution to this situation, Mr. Justice Holmes, speaking for the Court, said:

> "The defense under the Fourteenth Amendment is disposed of by what we have said. That under Article I, Section 10, needs but a few words more. One whose rights, such as they are, are subject to State restriction, cannot remove them from the power of the State by making a contract about them. The contract will carry with it the infirmity of the subject matter."

It is well at this point to dispel the impression which appellants have attempted to create in their brief that the decision of the New Jersey Court of Errors and Appeals in the instant case is at variance with its previous adjudications upon this subject. On the contrary, the high Court in New Jersey has repeatedly enunciated the principle that private contracts must yield to the paramount police power of the State when applied to economic conditions. Moreover, it has laid down this principle whether the legislation be of an emergency character or permanent, and its decisions are replete with pronouncements recognizing the force of the maxims hereinabove referred to. One of these decisions, *Veix v. Sixth Ward Building and Loan Association,* 123 N. J. L. 356, was affirmed in this Court in *Veix* v. *Sixth Ward Building and Loan Association,* 310 U. S. 31. Prior to the *Veix* case, however, the New Jersey Court decided *Bucsi* v. *Longworth Building and Loan Association,* 119 N. J. L. 120.

In that case, action was brought to recover the withdrawal value of ten installment shares of building and loan stock. The plaintiff rested her right of action upon the ground that she was entitled to payment according to the terms and provisions of the statute existing at the time she subscribed for the shares. The previous legislation in existence at the time of the purchase by plaintiff of her shares (and which is recited in detail in the Court's opinion) permitted withdrawals at book value at any time, upon thirty days' notice. By Chapter 102 of the Laws of 1932, the New Jersey Legislature had given matured shares a priority over withdrawing shareholders, and had provided further: "No withdrawal shall be paid if there are not funds sufficient to pay the matured shares on which payment has been requested thirty days after maturity." The Court indicated clearly that a radical change had been

effected in the rights and privileges of withdrawing shareholders. The plaintiff-appellant in the Court of Errors and Appeals of New Jersey did not challenge the prospective effect of the statute, but claimed that if retrospective, it violated her contract rights under Article I, Section 10, of the Federal Constitution. Chancellor Campbell, speaking for the New Jersey Court, said:

> "A legislative declaration of the existence of an emergency is entitled to judicial consideration but the courts must be guided by what is common knowledge. *Home Building and Loan Association* v. *Blaisdell*, 290 U. S. 398; 54 Sup. Ct. Rep. 231; 78 L. Ed. 413. • • •
>
> "But it is unnecessary to sustain the statute on the temporary ground that it is an emergency statute, because it is sustainable on broad constitutional grounds as a valid exercise of the reserved power of the state. This so-called reserved power is generally referred to as the police power of the state and extends to all great public needs. *Noble State Bank* v. *Haskell*, 219 U. S. 104, 110; 55 L. Ed. 112; 31 Sup. Ct. Rep. 486. • • •
>
> "It is well settled, however, that the constitutional interdiction against statutes impairing the obligation of contracts does not prevent the state from exercising such powers as are vested in it for the promotion of the common weal, or are necessary for the general good of the public, though contracts previously entered into may thereby be effected. *Home Building and Loan Association* v. *Blaisdell*, *supra* (at p. 437); *Manigault* v. *Springs*, 199 U. S. 473; 50 L. Ed. 274; 26 Sup. Ct. Rep. 127. • • •
>
> "This power is an attribute of sovereignty and all contracts are subject to its future exercise, and not only existing laws but also laws resulting from the exercise of this reserved power are read into

and made a part of all contracts. *Home Building and Loan Association* v. *Blaisdell, supra; Norman* v. *Baltimore and Ohio Railroad Co., et al.*, 294 U. S. 240; 79 L. Ed. 885; 55 Sup. Ct. Rep. 407; *Hourigan* v. *North Bergen, supra; People* v. *Title Mortgage and Guaranty Co., supra.* • • •

"Assuming that the appellant has a vested right of contract, the obligations on contract must yield to a proper exercise of the police power of the state and vested rights cannot inhibit the proper exercise of the power. *Home Building and Loan Association* v. *Blaisdell, supra. In Nebbia* v. *New York, supra* (at p. 523), Mr. Justice Roberts said:

"'Under our form of government the use of property and the making of contracts are normally matters of private concern. The general rule is that both shall be free from governmental interference. But neither property rights or contract rights are absolute; for government cannot exist if the citizen may, at his will, use his property right to the detriment of his fellows or exercise his freedom of contract to work them harm. Equally fundamental with the private right is that of the public to regulate it.'"

Commenting on the statute, the Court stated flatly:

"The statute denies a withdrawing shareholder a right to sue if the funds are applied as above stated. • • •

"The privilege of suit was granted to withdrawing members by the regulatory statutes of this state and it must be assumed that the legislature intended in granting the privileges of suit to withdrawing members that such a grant would be effective in carrying out the public interest affected upon which the regulation of the building and loan associations was predicated.

> "Experience has demonstrated that adverse economic conditions give the privilege of suit by a withdrawing member a legal force under our insolvency statutes which is absolutely destructive since the unrestricted exercise of the privilege of suit by such members was a motivating and inexorable force that eventually would have forced these associations into insolvency, forced the liquidation of their assets, with the resultant adverse effect upon vital public interests heretofore pointed out."

At another point in the opinion, the learned Chancellor says:

> "The contract was congenitally affected with a public interest and the contract carries with it the infirmity of the subject-matter. Rights which are subject to state restriction cannot be removed from the power of the state by the contract of the parties, nor can one legislature inhibit this power of the state to regulate or abridge the use of such contract rights when such use is destructive of vital public interests."

The Court also referred to and distinguished its decision in *Vanderbilt* v. *Brunton Piano Co.*, 111 N. J. L. 596, which is relied on by the appellants here. Chancellor Campbell said:

> "Nothing that has been said here should conflict with the holdings in *Vanderbilt* v. *Brunton Piano Co.*, 111 N. J. L. 596, and *Home Building and Loan Association* v. *Blaisdell, supra.* The subject-matter of the contracts in those cases was not per se affected with a public interest. The statutes there in question had effect only upon the interests of the respective contracting parties since the contracts affected thereby were of themselves only capable of a legal

or economic force which was co-terminous with the limits of the contract.

"The contract of the appellant, obviously, is not in the classification."

The same question came before the New Jersey Court of Errors and Appeals in *Veix* v. *Sixth Ward Building and Loan Association*, 123 N. J. L. 356, and the Court, upon the authority of its previous decision in *Bucsi* v. *Longworth Building and Loan Association, supra*, upheld the New Jersey legislation of 1932 (R. S. 17:12–53).* The Court said:

"The plaintiff-appellant says that the 1932 statute is invalid and the burden of the argument is that that statute is unconstitutional because it impairs the obligation of the contract, but we have already held to the contrary in the case of *Bucsi* v. *Langworth Building and Loan Association*, 119 N. J. L. 120, and *Rocker* v. *Cardinal Building and Loan Association*, 119 Id. 134, and this appeal is entirely controlled by our holding in those cases."

Veix v. *Sixth Ward Building and Loan Association, supra*, then reached this Court, 310 U. S. 32, and the constitutionality of the legislation in question was upheld in an opinion delivered by Mr. Justice Reed. Referring to the power of the State to regulate its building and loan associations, Justice Reed said:

"With institutions of such importance to its economy, the State retains police powers adequate to authorize the enactment of statutes regulating the withdrawal of shares. Unquestionably for the fu-

* The applicable sections of the New Jersey legislation relative to building and loan associations are printed at the end of this Brief in Appendix B.

ture, the provisions of the 1932 Act would be effective. *We think they were equally effective as to shares bought prior to the enactment of the statute,* notwithstanding the provisions of Article I, Section 10 of the Constitution that 'No State shall * * * pass any * * * Law impairing the obligation of contracts * * * ' This is so because the obligation of the Association to respond to the application for withdrawal was subject to the paramount police power. * * *.

"It was while statutory requirements were in effect that petitioner purchased his shares. When he purchased into an enterprise already regulated in the particular to which he now objects, he purchased subject to further legislation upon the same topic."

Discussing the economic conditions which necessitated legislative action, the Court said:

"An acceleration or a continuance of this tendency to withdraw available funds threatened a quick end to the ability of the institutions to meet even normal demands. Such threatened insolvency demands legislation for its control in the same way that liquidation after insolvency does. Such legislation may be classed as emergency in one sense but it need not be temporary. * * *.

"The fact that legislation was enacted during an emergency does not mean that it becomes unconstitutional when the emergency ceases where it concerns matter that may properly be the subject of permanent legislation."

Within the past year, these principles have been applied both by this Court and by the New Jersey tribunal. In *Gelfert* v. *National City Bank of New York*, 313 U. S. 221,

a New York statute providing, in substance, that in determining the amount of a deficiency judgment on the foreclosure of a mortgage, the Court should fix the "fair and reasonable market value" of the property and should deduct from the amount of the debt such market value, was held not to violate the contract clause of the Federal Constitution. Mr. Justice Douglas delivered the opinion of this Court and held that the statute was constitutional and was not an impairment of contract obligations in violation of the Federal Constitution, even as applied to a mortgage executed before the enactment of the statute, although, at the time of the execution of the mortgage, the law gave to the mortgagee the right to the full amount of the difference between the debt and the sale price at foreclosure sale. Mr. Justice Douglas said:

> "The formula which a legislature may adopt for determining the amount of a deficiency judgment is not fixed and invariable. That which exists at the date of the execution of the mortgage does not become so embedded in the contract between the parties that it cannot be constitutionally altered. As this Court said in *Home Bldg. & L. Asso.* v. *Blaisdell*, 290 U. S. 398, 435, 78 L. ed. 413, 427, 54 S. Ct. 231, 88 A. L. R. 1481, 'Not only are existing laws read into contracts in order to fix obligations as between the parties, but the reservation of essential attributes of sovereign power is also read into contracts as a postulate of the legal order.'"

Quoting the opinion of this Court in *Honeyman* v. *Hanan*, 302 U. S. 375, the Court said:

> "As stated by this Court in that case (302 U. S. at p. 378, 82 L. ed. 313, 58 S. Ct. 273), the Federal Constitution does not prevent the states from determining, on due notice and opportunity to be heard,

> 'by what process legal rights may be asserted or legal obligations' enforced. The principles of those cases are applicable here. The fact than an emergency was not declared to exist when this statute was passed does not bring within the protective scope of the contract clause rights which were denied such protection in *Honeyman* v. *Jacobs*, 306 U. S. 539, 83 L. ed. 972, 59 S. Ct. 702, *supra*. See *Home Bldg. & L. Asso.* v. *Blaisdell*, 290 U. S. 398, 78 L. ed. 413, 54 S. Ct. 231, 88 A. L. R. 1481, *supra*."

And finally, referring to the earlier decisions of the Court on the subject of impairment of contracts, Mr. Justice Douglas said:

> "We cannot permit the broad language which those early decisions employed to force legislatures to be blind to the lessons which another century has taught."

In *Veix* v. *Seneca Building and Loan Association*, 126 N. J. L. 314, decided April 3, 1941, the New Jersey Court of Errors and Appeals again held that a statute designed to meet an economic condition existing in the State was a valid exercise of the police power and did not impair the obligation of contract.

In that case, the Legislature had prescribed, by R. S. 17:12-53, the method and order to be employed by building and loan associations for the payment of maturities and withdrawals, and it had prohibited suit against such associations by any member thereof, to recover the maturity or withdrawal value so long as the funds in the treasury of the association are applied as required by the statute. The Court poses the following question: "Is this statute constitutional as applied to a member who, as plaintiff here, gave notice for the withdrawal value of his prepaid shares prior to its passage?"

The plaintiff's shares had a par value of $200 each and were issued with a provision that they should bear interest at 6 per cent, and that they might be called in and cancelled by the payment of "par value and interest to date of cancellation" to the owner. Plaintiff gave the building and loan association notice of the withdrawal in accordance with the law as it stood prior to the passage of the 1932 statute. The association refused to pay, basing its refusal upon this statute and upon Chapter 48 of the Laws of New Jersey of 1933 (R. S. App. A:7–3 to 7–7).*

The question before the Court was whether the acts of 1932 and 1933, precluding him from maintaining his suit, impaired the obligation of his contract with the association, contrary to the provisions of Article I, Section 10, of the Federal Constitution. It is important also to note that the plaintiff had given his notice of withdrawal three days before the effective date of the statute (Chapter 102, Laws of 1932, R. S. 17:12–53).

Mr. Justice Perskie, speaking for the New Jersey Court, said:

> "We know that we are dealing with 'financial institutions of major importance to the credit system of the state.' We know, without detailing the facts, that building and loan associations, including defendant association, could not by reason of their depreciated assets, owing to the prolonged period of the economic depression and lack of income, meet the heavy withdrawals. We know, as plaintiff was charged with knowing, that 'when he purchased into an enterprise already regulated in the particular to which he now objects, he purchased subject to further legislation upon the same topic.' * * *
>
> "But in our opinion neither the fact that plaintiff was the owner of prepaid shares, nor the fact that

* See Appendix C.

he gave notice before the passage of chapter 102, L. 1932, nor the combination of both circumstances, is the determinative test as to whether the statute is constitutional or unconstitutional.

"We have already held that the owner of prepaid shares who gave notice of withdrawal after the statutes became effective was not by chapter 102, L. 1932, deprived of any constitutional rights. *Veix* v. *Sixth Ward Building and Loan Association, supra.* We have held likewise when the owner of installment shares gave notice of withdrawal prior to the date when the statute became effective. *Bucsi* v. *Longworth Building and Loan Association,* 119 N. J. L. 120; 194 Atl. Rep. 857. And in the case of *Rocker* v. *Cardinal Building and Loan Association,* 13 N. J. Mis. R. 397; 179 Atl. Rep. 667; affirmed, 119 N. J. L. 134; 194 Atl. Rep. 865, which is strikingly similar to the instant case, there were present both prepaid shares and notice of withdrawal prior to the date when the statute became effective. In that case, too, we held that the statute deprived the holder of no constitutional rights. True, each share of stock in the *Roeker* case recited, on its face, that the 'annual profit of six per cent. per annum is guaranteed on these shares in lieu of all other profits payable semi-annually' and that the shares would be redeemed by the 'payment of maturity value thereof with such guaranteed profits to the date of redemption.' *The use of the words 'profit of six per cent.' and 'maturity value' instead of the words 'interest at six per cent.' and 'par value,' as in the instant case, does not constitute a sufficient basis for distinguishing the two cases, when, as here, the wording of both phrases obviously intended to, and did, in effect, convey the same meaning.*"

This language leaves no doubt whatever that the Court was passing upon legislation which required the holder of building and loan shares to accept security of a lesser value than that he had owned and paid for. He was required to withdraw his shares at "maturity value" instead of at "par value."

Mr. Justice Perskie finally grounded the decision of the Court upon the following proposition:

> "From all that has been written, it becomes increasingly clear that we have steadfastly adhered to the well recognized rule of law determinative of the constitutional exercise of the reserved police power of the state over property and contract rights. That rule of law is that every contract is made subject to the implied condition that its fulfillment may be frustrated by a proper exercise of the police power. But such a result can only be effected if the exercise of the power is for an end which is in fact public and the means adopted is reasonably adapted to that end. Cf. Indiana, *ex rel. Anderson* v. *Brand*, 303 U. S. 95, *108-*109; 82 L. Ed. 685, 695, and cases cited in footnote No. 17; *Nebbia* v. *New York*, 291 U. S. 502; 78 L. Ed. 940; *Veix* v. *Sixth Ward Building and Loan Association* (U. S.), *supra*, (at p. *44); 84 L. Ed. 1067. Contracts which relate, as here, to a subject-matter which lies within the control of the legislature, have a 'congenital infirmity' of being subject to the proper exercise of the police power. Cf. Gold Clause cases—*Norman* v. *Baltimore and Ohio Railroad Co.*, 294 U. S. 240; 79 L. Ed. 885; *Nortz* v. *United States*, 294 U. S. 317; 79 L. Ed. 907; *Perry* v. *United States*, 294 U. S. 330; 79 L. Ed. 912."

The considerations which motivated the Court in *Veix* v. *Seneca Building and Loan Association, supra*, as well

as in the other cases cited, are equally applicable to the instant case. In the *Veix* case, the Court was dealing with building and loan associations, designated by the Court as "financial institutions of major importance to the credit system of the State." Municipal corporations are of equal or greater importance as units in the government of the State, and their preservation and financial stability are vitally important to the welfare of their inhabitants and taxpayers and to their creditors. In the *Veix* case, the Court observed that owing to the prolonged period of economic depression, the associations could not meet heavy withdrawals, therefore, legislation was enacted to save the situation. The identical considerations applied in the case of the Municipal Finance Commission legislation. Over twenty-one hundred municipalities in the United States were in default on their bonds in 1932. This condition was widespread and the New Jersey Legislature was quick to recognize the fact. Widespread municipal default on bonded indebtedness, with indiscriminate suits and judgments, writs of mandamus requiring the raising of such judgments in municipal budgets, and the unchecked onset of creditors, might soon have wrecked the credit of all these municipalities. Abnormally high tax rates to pay such claims would simply have frustrated their own end, namely, the collection of taxes, because it is a well recognized principle in taxation that if the rate of taxation rises to a prohibitive point, property owners simply do not pay, properties are lost, and the aims of creditors seeking to collect on their claims are defeated. To prevent this complete economic collapse, the State of New Jersey enacted the legislation now the subject of review.

The cases above cited furnish abundant authority for the following propositions:

(a) The passage of the act was within the police power of the State;

(b) The rights of the holders of contracts, whether entered into before or after the passage of legislation, were subject to the exercise of this police power;

(c) The statute did not impair the obligation of contracts under Article I, Section 10, of the Federal Constitution.

POINT II.

Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937) is a lawful exercise of the police power, whether considered as an emergency measure or as permanent legislation.

While the legislation under discussion contained a provision declaring that it was designed to meet an emergency (R. S. 52:27–65), this is not a necessary element to render the legislation constitutional.

In view of the decisions cited in Point I of this brief, it is respectfully suggested that it is not necessary to reiterate them at length here. In *Gelfert* v. *National City Bank of New York*, 331 U. S. 221, 235, Mr. Justice Douglas said:

> "The fact that an emergency was not declared to exist when this statute was passed, does not bring within the protective scope of the contract clause rights which were denied such protection in *Honeyman* v. *Jacobs*, 306 U. S. 539."

In fact, the constitutionality of the legislation is grounded, not upon its emergency nature, but upon the reserve police power of the State. *Veix* v. *Seneca Building and Loan Association, supra; Veix* v. *Sixth Ward Building and Loan Association, supra.*

The declaration of an emergency strengthens the law and furnishes an additional reason for its validity. Viewed in either aspect, however, whether as an exercise of police power alone or as an exercise of police power designed to meet an emergency, the legislation is equally valid.

POINT III.

Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937) and Article 7 of Chapter 27 of Title 52 of the Revised Statutes of New Jersey (1937) do not deprive appellants of property without due process of law and do not deny to appellants the equal protection of the laws, nor abridge the privileges and immunities of citizens of the United States in violation of the Fourteenth Amendment to the Constitution of the United States.

The contention of appellants that the legislation under attack deprives appellants of property without due process of law and denies appellants the equal protection of the laws and abridges the privileges and immunities of citizens of the United States in violation of the Fourteenth Amendment to the Constitution of the United States is disposed of by the same decisions cited to dispose of the objection of appellants that the legislation impairs the obligation of contracts. The same principles of law and the same rationale are appropriate to meet both objections in the instant case. *Hudson County Water Company* v. *McCarter*, 209 U. S. 349.

The legislation enacted in New Jersey to regulate building and loan associations contains the same provisions changing the methods of enforcement of the obligation and restricting the right to institute suit as are embodied in the

legislation here under attack. And in the cases cited in Point I, that legislation has been upheld.

For these reasons, the cases there cited are not referred to again here, but are cited in answer to Point II of appellants' brief.

POINT IV.

The enactment by Congress of the Federal Municipal Bankruptcy Act of August 16, 1937, has no effect whatever upon the validity of the refunding proceeding consummated in Asbury Park pursuant to the State Statute.

The appellants argued in the State Court that when Congress adopted the Federal Municipal Bankruptcy Act in 1937, the New Jersey statute became inoperative and that the order of the Supreme Court of New Jersey authorizing the refunding plan of the City of Asbury Park to go into effect was therefore a nullity. They argue here that the Federal statute constitutes a bar to the enactment by the State of New Jersey of the legislation here under discussion and precludes any proceeding under it. They cite *United States* v. *Bekins*, 304 U. S. 27 (82 L. Ed. 1137), as authority for this contention. However, it requires only a careful reading of the *Bekins* case to demonstrate that there is no force whatever in this contention.

In 1934, Congress passed the first Municipal Bankruptcy Act. The United States Supreme Court in *Ashton* v. *Cameron County Water Improvement Company*, 298 U. S. 513, declared the act unconstitutional on the specific ground that it was an interference with State sovereignty. On August 16, 1937, the New Federal Municipal Bankruptcy Act was passed, and in *United States* v. *Bekins, supra*, this legislation was declared constitutional. The opinion of the Supreme Court by Chief Justice Hughes furnishes the answer

to the appellants' contention. The distinction between the two pieces of legislation was, in short, that the second act, unlike the first, is conditioned upon consent by the State. Mr. Justice Hughes quoted the report of the Committee on the Judiciary of the House of Representatives on the bill as follows:

> "The bill here recommended for passage expressly avoids any restriction on the powers of the states or their arms of government in the exercise of their sovereign rights and duties. No interference with the fiscal or governmental purposes of a political subdivision is permitted. *The taxing agency itself is the only instrumentality which can seek the benefits of the proposed legislation.* No involuntary proceedings are allowable and no control or jurisdiction over that property and those revenues of the petitioning agency necessary for essential governmental purposes is conferred by the bill."

The Chief Justice proceeds to analyze the statute as follows:

> "The statute is carefully drawn so as not to impinge upon the sovereignty of the state. The state retains control of its fiscal affairs. The bankruptcy power is exercised in relation to a matter normally within its province, *and only in a case where the action of the taxing agency, in carrying out a plan of composition approved by the bankruptcy court, is authorized by state law.*"

Discussing economic conditions from which had arisen the necessity for the legislation, the Chief Justice proceeds to observe:

> "The bankruptcy power is competent to give relief to debtors in such a plight, and, if there is

> no obstacle to its exercise in the case of the districts organized under state law, *it lies in the right of the state to oppose federal interference.* The state steps in to remove that obstacle. The state acts in aid and not in derogation of its sovereign powers. *It invites the intervention of the bankruptcy power to save its agency which the state itself is powerless to rescue.*"

These observations and this opinion by our highest Court make it clear that a Federal municipal bankruptcy statute which it is sought to invoke without the consent of the State is an infringement of State sovereignty. Such a statute, conditioned upon consent by the State, does not so infringe. On this ground, the second Federal Municipal Bankruptcy Act has been held constitutional, but nothing could be further from the fact than to allege that it supersedes the State legislation, or deprives the State of any inherent power it already possessed. In fact, a proceeding under the Federal act can only be set in motion with the consent of the State. *New Jersey has given that consent only where the Municipal Finance Commission authorizes application to the Federal Court in bankruptcy by the municipality concerned.* Section 83 (e) of the new bankruptcy act provides as a condition of confirmation of a plan of composition that it must appear that the petitioner was "authorized by law to take all action necessary to be taken by it to carry out the plan." In his opinion in the *Bekins* case, Chief Justice Hughes held that this required the consent of the State, and that it is "of the essence of sovereignty to be able to make contracts and give consents bearing upon the exertion of the governmental power." *United States* v. *Bekins*, 304 U. S. 27, 51.

New Jersey has guarded this right zealously, and in the Fort Lee refunding, while the litigation was pending

(*Borough of Fort Lee* v. *U. S., Ex Rel, Barker,* 104 F. (2d) 275), a proceeding for the refunding of the municipal debt was instituted under the new Federal Act, *upon the consent of the New Jersey Municipal Finance Commission.* In other words, the Borough of Fort Lee itself initiated the proceeding. No one could have forced it to avail itself of the benefit of the provisions of the legislation. Coupled with its application, it had, and of necessity, required the consent of the State agency, namely, the Municipal Finance Commission. Thus, it can readily be seen that it does not supersede the State legislation in which a creditor may make the application, nor was it ever intended so to do.

The matter of jurisdiction of the State and Federal Courts in the matter is analogous to that in the ordinary receivership and bankruptcy cases: A proceeding in receivership may be instituted in the State Court of Chancery despite the existence of the Federal bankruptcy law. If, during the pendency of that proceeding, bankruptcy ensues, the proceeding in the State tribunal is superseded, but this is not to say that the proceedings in the Chancery Court are inoperative merely because of the existence of another remedy—namely, a bankruptcy proceeding under the Federal statute. The same reasoning should be applied to the proceeding for the refunding of a municipal debt under the State law. Until a proceeding is instituted under the Federal act and with the necessary consent by the State, which must accompany such a proceeding, the Federal legislation is in no sense applicable nor operative.

Appellants take the position that the order of the New Jersey Supreme Court in the Asbury Park proceeding entered April 29, 1938, was a nullity, because the Federal legislation had been enacted August 16, 1937. However, the New Jersey Supreme Court had taken jurisdiction of the matter February 1, 1936, when the petition for ap-

proval of a plan of composition was filed, as shown by the affidavits on file in the motion to strike. It is as of that date that the statutory law, both State and Federal should be considered, and there was then no valid Federal municipal bankruptcy act in existence.

In conclusion on this point, it should be observed that if the position of the appellants were correct, then the existing outstanding new bonds to the extent of over $10,000,000.00, issued by the City of Asbury Park, would not be valid subsisting obligations of the city. It is not enough for the appellants to attempt to concede that the acceptance of these obligations by bondholders who exchanged their old bonds for new bonds renders them legal obligations. Obligations are legal only if legally issued. The Municipal Finance Commission of the State of New Jersey approved the proceeding for the issue of these new bonds and approved their issuance. Obviously, the Commission placed the same construction upon the applicability of the Federal legislation as is now placed upon it, and interpreted *United States* v. *Bekins, supra,* the way it is interpreted here.

Conclusion.

It remains to consider two cases cited by the appellants and the effect of an adverse decision upon the Asbury Park refunding operation and the bonds held by other bondholders.

Appellants cite *Sovereign Camp W. O. W.* v. *Wilentz,* 23 Fed. Supp. 23, as authority for the proposition that the legislation under discussion is unconstitutional. In that case, however, the Court, speaking through Judge Avis, specifically indicated that it was not passing upon the constitutionality of the legislation. The Court said:

> "We are not construing the Municipal Finance Commission Act of the State of New Jersey, its constitutionality, or its effect, except as the stays therein contained affect the right of the complainant to *enforce* its judgment."

The other case on this point cited by appellants (*State, ex rel. Phelps* v. *Fort Lee*, 14 N. J. Misc. 895) was to the same effect. In both cases, judgments had been secured before the municipalities were placed under the control of the Municipal Finance Commission, and the Courts, in the exercise of their discretion, awarded writs of mandamus to enforce the judgments obtained. Since that time, the New Jersey Court of Errors and Appeals (*Hourigan* v. *North Bergen Township, supra*) has held the stay provision constitutional. In the building and loan cases cited (*Veix* v. *Sixth Ward Building and Loan Association, supra*) this Court has held similar stay provisions constitutional. These decisions alone furnish a complete answer to appellants' contention.

Beyond this, however, in the instant case, no judgment has been secured and the question of the exercise of judicial discretion in the award of a writ of mandamus to enforce the judgment, is consequently not before the Court. For these reasons it will readily be seen that *Sovereign Camp W. O. W.* v. *Wilentz, supra*, and *State, ex rel. Phelps* v. *Fort Lee, supra*, are not in point.

It is difficult to follow the reasoning of the appellants to the effect that if the New Jersey legislation fails, the bonds issued pursuant to it, will not be invalid. Asbury Park issued bonds in the amount of $10,750,000.00 under its refunding plan and pursuant to the statute here under attack. The validity of those bonds undoubtedly depends on the validity of the legislation pursuant to which they were issued. Moreover, it will be readily observed from an

inspection of the city's refunding plan (R. 17), that a limitation is placed upon the amount to be raised for debt service each year. Obviously the tax rate of the city depends upon the debt service appropriation. If appellants were now to obtain judgment and were to enforce the judgment by a mandamus, the result would have to be the inclusion of the judgment of approximately $105,000.00 in the city's budget. This would sharply increase the tax rate and would disrupt the entire refunding plan to the great injury of the remaining bondholders. As a result of the application of the statute to the affairs of the city, order has been restored where there was chaos before. It is unquestionable that injury to the taxpayers, impairment of the value of property, and impairment of the market value of the securities held by the vast majority of the bondholders who accepted the plan, would result from the entry of a judgment which would enable appellants to collect in full. Moreover, the validity of the entire outstanding bond issues would be called in question with a consequent reduction in the value of those securities. It was to avoid all these conditions that the Legislature adopted the refunding law in New Jersey.

For the reasons herein urged, it is respectfully submitted that the judgment of the Court of Errors and Appeals of New Jersey, affirming the judgment of the Supreme Court of New Jersey, dismissing the appellants' complaint, should be affirmed.

Respectfully submitted,

WARD KREMER,
Attorney of Appellee.

APPENDIX A.

Pertinent Sections of Chapter 27 of Title 52 of the Revised Statutes of New Jersey.

52:27–2. **Petition to Supreme Court Justice alleging municipal default; procedure; commission to function.**

Whenever it shall be made to appear to a justice of the Supreme Court by any petition filed with him by or on behalf of the holder of any notes or bonds of any municipality of this State, verified by the petitioner, or his or its duly authorized agent, that such municipality has defaulted for over sixty days in the payment of the principal or interest of any of its outstanding notes or bonds held by the petitioner, the justice may make a summary investigation into the facts disclosed in the petition. For that purpose he may subpœna witnesses and call before him any officers of the municipality.

If it shall be established to the satisfaction of the justice that the municipality is so in default, he may make an order to that effect and file the same, together with the petition, in the office of the clerk of the Supreme Court.

Upon the filing of such order, together with the petition, the commission shall have and exercise with respect to such municipality the powers and duties prescribed by this chapter.

Sources. L. 1931, c. 340, § 101, p. 830, as am. by L. 1933, c. 9, § 1, p. 21. L. 1931, c. 340, § 102, p. 831, as am. by L. 1932, c. 236, § 1, p. 519, L. 1933, c. 330, § 1, p. 859.

52:27–3. **Resolution by municipality declaring inability to meet obligations; procedure before Supreme Court; commission to function.**

Any municipality may file with a justice of the Supreme Court a certified copy of a resolution adopted by the gov-

erning body of the municipality, reciting in general terms that due to unusual conditions the municipality is not in a position to meet its obligations when due, in spite of the endeavors of its officers, and petitioning that the commission shall function in the municipality.

Upon the filing of such petition and upon such notice to the commission as the justice may direct, the justice may make a summary investigation into the facts. For that purpose he may subpœna witnesses and call before him any officers of the municipality.

If it shall be established to the satisfaction of the justice that the municipality is so unable to meet its obligations, he may make an order to that effect and file the same, together with the petition, in the office of the clerk of the Supreme Court.

Upon the filing of such order, the commission shall function in such municipality with all the powers and duties conferred by this chapter.

Sources. L. 1931, c. 340, § 103, p. 831, as am. by L. 1933, c. 330, § 2, p. 860.

52:27-4. **Duration of commission in municipality; subsequent powers of State Auditor.**

The commission shall continue in force in such municipality, and shall exercise the powers and perform the duties conferred by this chapter until all bonds or notes or other indebtedness of the municipality which has fallen due, and all bonds or notes which will fall due within one year, and the interest thereon, have been paid or funded or refunded, or the payment thereof in cash adequately provided for by a cash reserve, excepting tax anticipation or tax revenue notes or bonds of the current year, at which time its authority under this chapter shall cease.

Thereafter the State Auditor shall have the power to continue the employment of the auditor as provided for in Section 52:27-6 of this Title and to exercise the powers of

the commission under Section 52:27–22 of this Title, until the gross and net debt of such municipality, including notes or bonds issued under this chapter, is within all statutory limits, at which time his authority under this chapter shall cease.

Source. L. 1931, c. 340, § 403, p. 835, as am. by L. 1933, c. 330, § 10, p. 865.

52:27–8. **Office for auditor; access to books and records.**

The auditor employed by the commission shall have an adequate office in the municipal building, if any, and shall have access to all books of account, records, papers and memoranda of such municipality.

Source. L. 1931, c. 340, § 302, p. 834.

52:27–9. **Warrants and checks to be countersigned by auditor.**

All warrants, checks or other instruments for the withdrawal or transfer of funds of the municipality shall be submitted to such auditor for his countersignature, and no banking institution in which funds of the municipality have heretofore been or shall hereafter be deposited shall honor warrants or checks drawn thereon unless the countersignature of such auditor shall appear on the face of such instruments.

Source. L. 1933, c. 330, § 7(302a), p. 863 (amendment), suppl. to L. 1931, c. 340, p. 830.

52:27–13. **Commission may carry out directions not complied with by municipality.**

Whenever any direction of the commission authorized under this chapter has not been fully performed or carried out by the officials of the municipality affected, the commission may perform directly, or cause to be performed by its agents, in the name of the municipality, any act so directed by the commission, including the power to execute, sell, issue and deliver any bonds or notes directed

to be issued under a resolution certified in accordance with Section 52:27–14 of this Title.

Source. L. 1931, c. 340, § 402, p. 834.

52:27–13.3. **Special collectors; appointment.**

Whenever, pursuant to this chapter, the commission shall function in a municipality, it shall have, in addition to the powers granted in Sections 52:27–13.1 and 52:27–13.2 of this Title, the power by resolution to recommend to the governing body of such municipality the appointment of one or more persons to act as special collectors of delinquent taxes or any other revenues in such municipality. Thereupon it shall be the duty of the governing body, with the concurrence and approval of the commission, to appoint a person or persons satisfactory to the governing body and to the commission to act as such special collector or collectors and to fix his or their compensation, and it shall be lawful so to appoint a person or persons residing outside of the municipality.

Source. L. 1935, c. 292, § 4, p. 928, suppl. to L. 1931, c. 340, p. 830.

52:27–14. **Funding or refunding indebtedness; resolution by commission.**

The commission may from time to time prepare and certify to the governing body of any municipality in which the commission is functioning, resolutions providing for the funding or refunding of notes or bonds, or other indebtedness of the municipality, and the interest thereon, which the commission shall have found after public hearing to be outstanding and unpaid and to be due or to become due.

Source. L. 1931, c. 340, § 201, p. 831, as am. by L. 1932, c. 236, § 3, p. 519, L. 1935, c. 192, § 1, p. 467.

52:27-20. **Public sale of notes or bonds; exceptions.**

All such notes or bonds shall be sold at not less than par at public sale after notice setting forth the terms and conditions of sale, published in such newspaper circulating in the municipality, and in such financial newspaper, as shall be designated by resolution, except in the following cases:

a. If no bids are received at such public sale, or if all bids are rejected, any notes or bonds or part thereof may with the written assent of the commission be sold without further notice at private sale at any time within six months.

b. With the approval in writing of the commission, any notes or bonds or part thereof may be exchanged for any notes or bonds, including interest thereon, of the municipality issued under this or any other law. The rate of interest borne by any such notes or bonds may be higher or lower than the rate of interest borne by the notes or bonds surrendered.

Source. L. 1931, c. 340, § 207, p. 832, as am. by L. 1932, c. 236, § 6, p. 520.

52:27-32.1. **Enforcement of judgments, etc., against municipality stayed; necessity of court order.**

Whenever the commission shall function in any municipality and so long as it shall continue so to do, no judgment, decree, levy or execution against the municipality or the property thereof for the recovery of the amount due on any bonds, notes or other obligations of the municipality, in the payment of which the municipality has defaulted, shall be enforced until otherwise specially ordered by the Supreme Court or a justice thereof in an appropriate proceeding for such purpose, after notice to the commission, and the enforcement of any such judgment, decree, levy or execution shall be stayed until otherwise specially ordered as aforesaid.

Source. L. 1932, c. 236, § 16(351), p. 526 (amendment) as am. by L. 1933, c. 330, § 8, p. 863, suppl. to L. 1931, c. 340, p. 830.

52:27-34. **Petition by creditors; plan of adjustment or composition; parties; notice.**

Upon the verified petition of any creditors of a municipality in which the commission shall function, made on behalf of themselves and all other creditors of the municipality, for the approval of a plan of adjustment or composition of the claims of all creditors or of a class or classes of them similarly situated, which plan shall be submitted with and made a part of the petition, the Supreme Court by a justice thereof may take jurisdiction of the subject matter and order the filing of the petition in the office of the clerk of the Supreme Court.

The municipality and the commission shall be made parties to such proceeding. All creditors of the municipality shall be made parties thereto by notice to be published and given in such manner as the Supreme Court by its justice may direct. Any creditor of the municipality may appear and assert his rights.

Source. L. 1933, c. 331, § 1, p. 866, suppl. to L. 1931, c. 340, p. 830.

52:27-35. **Allegations in petition.**

In the petition the creditors shall allege that the municipality is or will be unable to pay in full according to their terms the claims proposed to be adjusted or composed and perform its public functions and preserve the value of property subject to taxation, that the adjustment or composition proposed in the plan is substantially measured by the capacity of the municipality to pay, is in the interests of all the creditors affected thereby, and is not detrimental to other creditors of the municipality.

Source. L. 1933, c. 331, § 1, p. 866, suppl. to L. 1931, c. 340, p. 830.

52:27-36. **Approval by Supreme Court Justice of plan of adjustment or composition; findings.**

In any such proceeding, after hearing on the plan proposed or on the plan as modified by order and if such plan as proposed or modified is approved in writing by creditors representing eighty-five per cent in amount of the indebtedness affected thereby and by the municipality and the commission, the Supreme Court by a justice thereof may by order authorize and approve such adjustment or composition if the Court by its justice determines (1) that the municipality is unable to pay in full according to their terms the claims proposed to be adjusted or composed, and perform its public functions, and preserve the value of property subject to taxation, (2) that the adjustment or composition is substantially measured by the capacity of the municipality to pay, (3) that it is in the interest of all the creditors affected thereby, and (4) that it is not detrimental to other creditors of the municipality.

Source. L. 1933, c. 331, § 2, p. 867, suppl. to L. 1931, c. 340, p. 830.

52:27-37. **Approved plan binding on all creditors; substituted obligations.**

The plan of adjustment so authorized and approved shall forthwith and without any further action of any kind be binding upon all the creditors included in the plan, whether or not they appear in the proceeding. In so far as said plan provides for the substitution of any new bonds, notes or other obligations of the municipality in place of any outstanding bonds, notes or other obligations, or claims then outstanding, such substitution shall be effectual from and after such date as may be fixed in such order.

Source. L. 1933, c. 331, § 3, p. 867, suppl. to L. 1931, c. 340, p. 830.

52:27-38. **Continuance of stay of proceedings against municipality; action by creditor to enforce claim restricted.**

After the institution of any proceeding provided for by this article and pending the determination thereof, the Supreme Court by a justice thereof may by order continue the stay provided by Sections 52:27-32.1 and 52:27-33 of this Title.

In the event that a plan shall be authorized and approved pursuant to this article the Court shall retain jurisdiction of such proceeding and thereafter no creditor whose claim is included in such adjustment or composition shall be authorized to bring any action or proceeding of any kind or character for the enforcement of his claim except with the permission of the Supreme Court and then only to recover and enforce the rights given him by the adjustment or composition.

Source. L. 1933, c. 331, § 4, p. 867, suppl. to L. 1931, c. 340, p. 830.

52:27-39. **Reduction in principal of outstanding notes or bonds prohibited.**

Notwithstanding any provisions of this article, the commission shall not approve any adjustment or composition, or plan presented pursuant to this article, which provides for the reduction in the principal amount of any outstanding notes or bonds of the municipality.

Source. L. 1933, c. 331, § 5, p. 868, suppl. to L. 1931, c. 340, p. 830.

52:27-65. **Remedial law to meet public emergency; liberal construction.**

It is declared that this chapter is intended by the Legislature to meet the public emergency arising from a default in the payment of municipal and school district obligations and the resulting impairment of public credit, requiring intervention by the State to provide for the payment of existing obligations in such a way as to cause the least

embarrassment to property owners as taxpayers, and that this chapter is remedial in nature and the powers hereby granted shall be liberally construed.

Sources. L. 1931, c. 340, § 405, p. 835. L. 1935, c. 258, § 20, p. 838, suppl. to L. 1903 (2d Sp. Sess.) c. 1, p. 5.

APPENDIX B.

Pertinent Sections of New Jersey Legislation Regulating Building and Loan Associations Laws of 1925, Chapter 65.

Article III, Sec. 49 (P. L. 1925, p. 211).

1. Withdrawal of Shares.

49. **How withdrawn.**

The shares of every such association of this State, or doing business therein, may be withdrawn by the holder at any time, by giving such written notice as may be provided for in the constitution or by-laws, not to exceed thirty days; if the withdrawal be made within the first year, the withdrawal value of the shares withdrawn shall be not less than the sum of the subscription or dues paid on such shares, less a proportionate share of any loss sustained by such association; after the first year a reasonable share of the profits less unpaid fines shall be included in the withdrawal value; in case such shares are pledged as collateral security for the repayment of a loan made thereon by such association, the amount of such loan shall be deducted from such withdrawal value and the difference only paid to such member; amounts paid for salaries, commissions and other current expenses shall not be considered losses within the meaning of this section.

Article III, Sec. 52 (P. L. 1925, p. 212).

52. **Payment of withdrawals.**

Withdrawals from any such association shall be paid in the order in which the notices thereof shall have been received, but not more than one-half of the receipts of any one month shall be required to be used for the payment of withdrawal claims, without the consent of the board of directors, until the oldest of such claims then unpaid shall have been on file for a period of six months; but in no case shall payment be postponed for a period longer than six months from the date of such notice, and any member who has given the said notice may sue for and recover the withdrawal value of his shares in any such association in any court of competent jurisdiction, if the same is not paid in six months from the date of the giving of said notice of withdrawal.

Article 7 of Chapter 12 of Title 17 of the Revised Statutes of New Jersey.

17:12-49. **Withdrawal of shares.**

The shares of every building and loan association of this State, or doing business herein, may be withdrawn by the holder upon giving such written notice, not exceeding thirty days, as its constitution provides. Upon withdrawal of such shares a reasonable portion of the dividends or profits, if any, credited to such shares may be retained by such association and the remainder of the amounts credited on such shares, less fines and other obligations thereon, paid to the withdrawing member in the manner otherwise provided in this chapter, but no fines shall be deducted from the dues credited on shares which shall be withdrawn within one year after such shares shall have been subscribed. This section shall not be construed to prevent a reduction of the share liability of any such association to its members for the purpose of providing for losses or anticipated losses

or of reserving against them as otherwise provided in this chapter. The commissioner, if it appears to him that the association is in an unliquid condition, may authorize the making of a written agreement, which shall be binding on assenting members of the association, whereby the assenting members shall agree not to file a notice of withdrawal before a date specified in the agreement. Notice of the agreement shall be printed or stamped upon the face of the certificate or pass book, or both, of each assenting member when the certificate or pass book comes into the possession of the association.

Source. L. 1925, c. 65, § 49, p. 211, as am. by L. 1932, c. 92, § 1, p. 161; L. 1935, c. 59, § 10, p. 152.

17:12-53. **Payment of maturities and withdrawals.**

Maturities and withdrawals shall be paid in the manner and subject to the limitations provided herein.

a. Maturities shall be paid in the order in which they become due except as provided herein and withdrawals shall be paid in the order in which notices of withdrawal shall have been filed except as provided herein; and

b. The maturities of any one month shall be paid before the maturities of subsequent months; and

c. One-third of the net receipts of any such association in each fiscal month shall be made available so far as necessary for the payment of maturities or for the establishing of maturity reserves and another one-third of the net receipts of any such association in each fiscal month shall be made available so far as necessary for the payment of withdrawals; and the words "net receipts," as used in this section, shall be construed to mean the moneys, other than borrowed moneys, received by any such association less moneys used for operating expenses, moneys used to pay creditor obligations, moneys used for the conservation, preservation or protection of the property and assets of such association, and moneys reserved for any of such purposes; and

d. If at the end of any fiscal month the funds of any such association required to be made available for the payment of withdrawals, together with such other funds, if any, made available for such purpose by the board of directors, shall be insufficient for the payment of all withdrawals then due and payable, the board of directors of such association shall, so far as possible, pay out of such funds, on account of the sum due to each member who has filed notice or notices of withdrawal, without regard to the fact that such notice or notices shall have been filed by such member on more than one share account, in the order in which such notices shall have been filed, the sum of fifty dollars or the balance due to such member, whichever is less and, if the available funds shall not thereby be exhausted or become inadequate, shall, so far as possible, again pay on account of the sum due to each such withdrawing member, in said order, the sum of fifty dollars or the balance due to such member, whichever is less, and shall repeat the process until the available funds shall become inadequate or exhausted; and subsequent available funds, when available, shall be applied to the payment of then existing withdrawal obligations in the same manner beginning with the withdrawal of the member next following the one on whose account the last such payment was made; and, in the event, that such member shall have filed more than one notice of withdrawal, his place in the order of payment shall be as of the date and time of the first notice filed by him; and

e. No member to whom any such association shall be obligated for the payment of any maturity or withdrawal shall have the right to bring suit against such association to recover the maturity or withdrawal value of his shares or any part thereof so long as the funds of such association shall be applied as required by this section; and

f. The board of directors of any such association shall have the right, in its discretion, to make available additional funds other than those required in paragraph "e" of this section for the payment of maturities and with-

drawals; but no more than one-third of the net receipts as defined in said paragraph "c" shall be used for the payment of withdrawals while maturities remain unpaid. Borrowed moneys shall not be used for the payment of withdrawals while maturities remain unpaid.

Source. L. 1925, c. 65, § 52, p. 212, as am. by L. 1932, c. 102, § 1, p. 175; L. 1935, c. 59, § 11, p. 153, L. 1936, c. 118, § 4, p. 295.

APPENDIX C.

Revised Statutes of New Jersey,

Chapter 7.

App. A:7–3. **Additional powers enumerated.**

1. The Commissioner of Banking and Insurance shall have power, in addition to such other powers as he may have, notwithstanding the provisions of the act to which this act is a supplement and the amendments and supplements thereof, from time to time, to make orders for the purpose of conserving the assets of the building and loan associations of this State, which orders shall have the same force and effect as law and be binding on any and/or all building and loan associations of this State, whereby:

(a) to regulate the method of paying the withdrawal value and/or maturity value of shares of any and/or all of such associations;

(b) to regulate and/or postpone the filing of applications for withdrawal of shares and of requests for payment of maturity value of shares of any and/or all such associations;

(c) to regulate or postpone the payment of all or any part of the maturity value or of the withdrawal value of shares of any and/or all such associations;

(d) to require any and/or all such associations to establish additional reserves or increase present reserves and to regulate any reserves of any and/or all such associations

and to prescribe the manner in which such reserves shall be established;

(e) to regulate, allocate, prohibit or postpone the receipt and/or disbursement of funds by any such associations;

(f) to effect such changes and/or reorganization in the business and/or affairs of any and/or all such associations as he shall deem necessary or proper;

(g) Whenever it is essential, in the public interest, to appoint under his hand and official seal one or more conservators to assist him in the operation of the business of any building and loan association in this State and such conservator shall execute such changes and/or reorganization in the business and/or affairs of any such association as may be directed by the commissioner; and shall be subject to such orders or regulations as issued or may hereafter be issued by the commissioner pursuant to the provisions of this act. The commissioner may require of such conservator such bond and security as he deems proper. The conservator, under the direction of the commissioner, shall take possession of the books, records and assets of every description of such association, and take such action as may be necessary to conserve the assets of such association pending further disposition of its business as provided by law. Such conservators shall have all the rights, powers and privileges now possessed by or hereafter given receivers of corporations organized and existing under the laws of this State, and in addition thereto, the right to renew and/or pay on account of maturing creditor obligations, and to secure the same if necessary, and the further right and power to incur new obligations, if in the interest of said association, and shall be subject to the obligations and penalties not inconsistent with the provisions of this act to which said conservators are now or may hereafter become subject; provided, however, that said conservators shall not have the power to liquidate any such association. During the time that such conservator remains in posses-

sion of such association, the rights of all parties with respect thereto shall, subject to the provisions of this subchapter, be the same as if a receiver had been appointed therefor. All expenses of any such conservatorship shall be paid out of the assets of such association and shall be a lien thereon, which shall be prior to any other lien. The commissioner shall fix the compensation of such conservator and of such persons employed by him in the performance of his duties, which compensation shall be disbursed from the funds of such association. If the commissioner becomes satisfied that it may safely be done and that it would be in the public interest, he may, in his discretion terminate the conservatorship and permit such association to resume the transaction of its business, subject to such terms, conditions, restrictions and limitations as he may prescribe, in which event said association shall become revested with title to all the real and personal property wherever situated. (L. 1933, c. 48, § 1, p. 94, as am. by L. 1933, c. 166, § 1, p. 346, L. 1933, c. 258, § 1, p. 694, L. 1933, c. 381, § 1, p. 1068, suppl. to L. 1925, c. 65, p. 189.)

App. A 7-4. **Commissioner not liable in damages.**

2. The commissioner shall not be liable in damages to any person by reason of errors of judgment in carrying out the powers herein conferred on him nor shall he be liable in damages for failure to act under said powers. (L. 1933, c. 48, § 2, p. 95, as am. by L. 1933, c. 166, § 2, p. 348, L. 1933, c. 258, § 2, p. 696, L. 1933, c. 381, § 2, p. 1070, suppl. to L. 1925, c. 65, p. 189.)

App. A 7-5. **Commissioner may modify, suspend or revoke orders.**

3. The commissioner shall have authority to repeal, suspend or modify any order made by him pursuant to the provisions of this law. (L. 1933, c. 48, § 3, p. 95, as am. by L. 1933, c. 166, § 3, p. 348, L. 1933, c. 258, § 3, p. 696. L. 1933, c. 381, § 3, p. 1070, suppl. to L. 1925, c. 65, p. 189.)

App. A:7-6. **Orders effective, when.**

4. No order made hereunto nor any suspension, modification or repealer thereof shall be effective until a copy thereof shall be filed in the Department of Banking and Insurance and a copy thereof delivered or mailed to the association or associations affected. (L. 1933, c. 48, § 4, p. 95, as am. by L. 1933, c. 166, § 4, p. 348, L. 1933, c. 258, § 4, p. 696, L. 1933, c. 381, § 4, p. 1070, suppl. to L. 1925, c. 65, p. 189.)

App. A:7-7. **Duration of act, operative effect of orders continued.**

This act shall take effect immediately, but shall become inoperative after September fifth, one thousand nine hundred and forty, but all orders or regulations made and all acts and things done under the provisions of this act shall be and remain valid and operative. (L. 1933, c. 48, § 5, p. 95, as am. by L. 1933, c. 166, § 5, p. 348, L. 1933, c. 258, § 5, p. 696, L. 1933, c. 381, § 5, p. 1071, L. 1936, c. 119, § 1, p. 300, L. 1937, c. 41, § 1, p. 87, L. 1938, c. 110, p. 231, § 1, L. 1939, c. 128, p. 437, § 1, suppl. to L. 1925, c. 65, p. 189.)

SUPREME COURT OF THE UNITED STATES.

No. 896.—October Term, 1941.

Faitoute Iron & Steel Company, The Howard Savings Institution, Florence W. Faitoute, et al., Appellants, *vs.* City of Asbury Park, A Municipal Corporation of the State of New Jersey.	Appeal from the Court of Errors and Appeals of the State of New Jersey.

[June 1, 1942.]

Mr. Justice Frankfurter delivered the opinion of the Court.

A New Jersey statute, adopted in 1931, authorized state control over insolvent municipalities. By a supplementary law, enacted in 1933, a plan for adjustment of the claims of creditors of such an insolvent municipality could be made binding upon all creditors. The question is whether an adjustment so authorized by a state impairs rights in violation of the Constitution of the United States.

The City of Asbury Park is a seashore resort with a resident population of 15,000. It presents a familiar picture of optimistic and extravagant municipal expansion caught in the destructive grip of general economic depression: elaborate beachfront improvements, costs in excess of estimates, deficits not annually met by taxation, declining real-estate values, inability to refinance a disproportionately heavy load of short-term obligations, and, inevitably, default. Accordingly, in January, 1935, availing themselves of the New Jersey Municipal Finance Act, creditors applied to the Supreme Court of New Jersey to place the state Municipal Finance Commission in control of the city's finances.

The legislation was enacted "to meet the public emergency arising from a default in the payment of municipal obligations, and the resulting impairment of public credit", Laws of New Jersey (1931), c. 340, § 105. In broad terms, the legislation, through combined administrative and judicial action, adapted the underlying principles of an equity receivership to the solution of the problem of insolvent municipalities. By a supplementing act,

Laws of New Jersey (1933), c. 331, a "plan of adjustment or composition of the claims of all creditors" may be submitted on their behalf to the supreme court of the state. If approved by 85 per cent in amount of the creditors and by the municipality and the Commission, such plan of adjustment may be adopted "if the court by its justice determines (1) that the municipality is unable to pay in full according to their terms the claims proposed to be adjusted or composed, and perform its public functions and preserve the value of property subject to taxation, (2) that the adjustment or composition is substantially measured by the capacity of a municipality to pay, (3) that it is in the interest of all the creditors affected thereby, and (4) that it is not detrimental to other creditors of the municipality." The plan cannot be authorized, however, if it involves any reduction of the principal amount of any outstanding obligation. Any creditor is entitled to appear and to be heard, but a plan which is so authorized by the court is binding upon all creditors whether or not they appear, and the substitution of new obligations for old in carrying out the plan is made effective from the day fixed by judicial order. To effectuate such a plan, the Act provides further that the court shall retain jurisdiction and "thereafter no creditor whose claim is included in such adjustment or composition shall be authorized to bring any action or proceeding of any kind or character for the enforcement of his claim except with the permission of the supreme court and then only to recover and enforce the rights given him by the adjustment or composition."[1]

[1] The text of the legislation as incorporated in N. J. Revised Statutes (1937), tit. 52, c. 27, indicates the careful character of the legislation:

"52:27-34. Petition by creditors; plan of adjustment or composition; parties; notice. Upon the verified petition of any creditors of a municipality in which the commission shall function, made on behalf of themselves and all other creditors of the municipality, for the approval of a plan of adjustment or composition of the claims of all creditors or of a class or classes of them similarly situated, which plan shall be submitted with and made a part of the petition, the supreme court by a justice thereof may take jurisdiction of the subject matter and order the filing of the petition in the office of the clerk of the supreme court.

"The municipality and the commission shall be made parties to such proceeding. All creditors of the municipality shall be made parties thereto by notice to be published and given in such manner as the supreme court by its justice may direct. Any creditor of the municipality may appear and assert his rights.

"52:27-35. Allegations in petition. In the petition the creditors shall allege that the municipality is or will be unable to pay in full according to their terms the claims proposed to be adjusted or composed and perform its

Pursuant to this legislative scheme, the City of Asbury Park was on March 7, 1935, placed under the control of the Municipal Finance Commission; on February 1, 1936, a plan for the refunding of its bonded debt was filed in the state supreme court, and that court took jurisdiction of the proceedings; the plan, as amended, was approved by the court on July 21, 1937; on September 28, 1937, it was duly approved by the Municipal Finance Commission; on April 29, 1938, it was consented to by creditors representing "85 per cent in amount of the indebtedness affected"

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public functions and preserve the value of property subject to taxation, that the adjustment or composition proposed in the plan is substantially measured by the capacity of the municipality to pay, is in the interests of all the creditors affected thereby, and is not detrimental to other creditors of the municipality.

"52:27-36. Approval by supreme court justice of plan of adjustment or composition; findings. In any such proceeding, after hearing on the plan proposed or on the plan as modified by order and if such plan as proposed or modified is approved in writing by creditors representing eighty-five per cent in amount of the indebtedness affected thereby and by the municipality and the commission, the supreme court by a justice thereof may by order authorize and approve such adjustment or composition if the court by its justice determines (1) that the municipality is unable to pay in full according to their terms the claims proposed to be adjusted or composed, and perform its public functions and preserve the value of property subject to taxation, (2) that the adjustment or composition is substantially measured by the capacity of the municipality to pay, (3) that it is in the interest of all the creditors affected thereby, and (4) that it is not detrimental to other creditors of the municipality.

"52:27-37. Approved plan binding on all creditors; substituted obligations. The plan of adjustment so authorized and approved shall forthwith and without any further action of any kind be binding upon all the creditors included in the plan, whether or not they appear in the proceeding. In so far as said plan provides for the substitution of any new bonds, notes or other obligations of the municipality in place of any outstanding bonds, notes or other obligations, or claims then outstanding, such substitution shall be effectual from and after such date as may be fixed in such order.

"52:27-38. Continuance of stay of proceedings against municipality; action by creditor to enforce claim restricted. After the institution of any proceeding provided for by this article and pending the determination thereof, the supreme court by a justice thereof may by order continue the stay provided by sections 52:27-32.1 and 52:27-33 of this title.

"In the event that a plan shall be authorized and approved pursuant to this article the court shall retain jurisdiction of such proceeding and thereafter no creditor whose claim is included in such adjustment or composition shall be authorized to bring any action or proceeding of any kind or character for the enforcement of his claim except with the permission of the supreme court and then only to recover and enforce the rights given him by the adjustment or composition.

"52:27-39. Reduction in principal of outstanding notes or bonds prohibited. Notwithstanding any provisions of this article the commission shall not approve any adjustment or composition, or plan presented pursuant to this article, which provides for the reduction in the principal amount of any outstanding notes or bonds of the municipality."

by the plan; and, on June 15, 1938, it was put into operation. The plan provided for the refunding of $10,750,000 of outstanding bonds; these were to be exchanged by the consenting creditors for new bonds to be issued in accordance with the terms of the plan approved by the court.

The appellants were holders of defaulted bonds and interest coupons issued by the City of Asbury Park in 1929 and 1930—prior, therefore, to the legislation which authorized the proceedings resulting in the challenged refunding scheme. The bonds of the appellants were part of the $10,750,000 of refunded bonds which, under the adjustment decreed by the court, could only be converted into new bonds maturing in 1966 and bearing a lower rate of interest than the original bonds. Deeming the arrangement authorized under the New Jersey statute to be violative of the Constitution of the United States, the appellants brought this suit for the face value of the old bonds and coupons. The Supreme Court of New Jersey dismissed the suit, 19 N. J. Misc. 322; the Court of Errors and Appeals affirmed the dismissal, 127 N. J. L. 239; and the case is here on appeal under § 237(a) of the Judicial Code, as amended, 28 U. S. C. § 344.

If the New Jersey legislation which is the foundation of the refunding plan for the City of Asbury Park is valid, appellants' claim on the old bonds was barred by law, and the judgment below must stand. The validity of that legislation is assailed on two grounds. It is contended, first, that the New Jersey laws constitute municipal bankruptcy legislation, that that field of lawmaking has been preempted by Congress, and that the New Jersey legislation is therefore inoperative. To this argument a few dates furnish a short answer. The present court proceedings began on February 1, 1936. The first federal Municipal Bankruptcy Act was declared unconstitutional on May 25, 1936. *Ashton* v. *Cameron County Dist.*, 298 U. S. 513. The refunding plan now assailed was approved, as we have seen, on July 21, 1937. It was thus authorized more than a year before the enactment of the only relevant federal statute, the Act of August 16, 1937, 50 Stat. 653, amending the Bankruptcy Act to provide for the composition of indebtedness of taxing agencies. Assuming Congress had power to do so, this Act did not profess to terminate a pending state court proceeding like that now in question. It would offend the most settled habits in the relationship between the States and the

nation to imply such a retroactive nullification of state authority over its subordinate organs of government.

We prefer, however, to dispose of this objection on a broader ground. Not until April 25, 1938, was the power of Congress to afford relief similar to that given by New Jersey for its municipalities clearly established, *United States* v. *Bekins*, 304 U. S. 27, and then only because Congress had been "especially solicitous to afford no ground" for the "objection" that an exercise of federal bankruptcy over political subdivisions of the State "might materially restrict its control over its fiscal affairs" whereby states would no longer be "free to manage their own affairs". The statute was "carefully drawn so as not to impinge on the sovereignty of the State. The State retains control of its fiscal affairs. The bankruptcy power is exercised . . . only in a case where the action of the taxing agency in carrying out a plan of composition approved by the bankruptcy court is authorized by state law." 304 U. S. at 50, 51. New Jersey expressly prohibits any municipality to avail itself of a federal bankruptcy act "unless the approval of the municipal finance commission . . . be first had and obtained". Revised Statutes of New Jersey (1937), 52:27-40. The City of Asbury Park has never attempted to resort to a federal bankruptcy court, and the New Jersey Municipal Finance Commission has not authorized it to do so. Can it be that a power that was not recognized until 1938, and when so recognized, was carefully circumscribed to reserve full freedom to the states, has now been completely absorbed by the federal government—that a state which, as in the case of New Jersey, has after long study devised elaborate machinery for the autonomous regulation of problems as peculiarly local as the fiscal management of its own household, is powerless in this field? We think not.

This brings us to the second and main contention, namely, that the appellants' claims in the form of the bonds and coupons issued by the City of Asbury Park, constituted contracts, the obligation of which is impaired by the denial of their right to recover thereon and by their transmutation, without their consent, into the securities authorized by the plan of adjustment.

The principal asset of a municipality is its taxing power and that, unlike an asset of a private corporation, can not be available for distribution. An unsecured municipal security is therefore merely a draft on the good faith of a municipality in exer-

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cising its taxing power. The notion that a city has unlimited taxing power is, of course, an illusion. A city cannot be taken over and operated for the benefit of its creditors, nor can its creditors take over the taxing power. Indeed, so far as the federal Constitution is concerned, the taxing power of a municipality is not even within its own control—it is wholly subordinate to the unrestrained power of the state over political subdivisions of its own creation. "A municipal corporation . . . is a representative not only of the State, but is a portion of its governmental power . . . . The State may withdraw these local powers of government at pleasure, and may, through its legislature or other appointed channels, govern the local territory as it governs the State at large. It may enlarge or contract its powers or destroy its existence." *United States* v. *Railroad Company*, 17 Wall. 322, 329. And see *Hunter* v. *Pittsburgh*, 207 U. S. 161.

In effect, therefore, the practical value of an unsecured claim against the city is inseparable from reliance upon the effectiveness of the city's taxing power. The only remedy for the enforcement of such a claim is a mandamus to compel the levying of authorized taxes. The experience of the two modern periods of municipal defaults, after the depressions of '73 and '93, shows that the right to enforce claims against the city through mandamus is the empty right to litigate. See Hillhouse, *Lessons from Previous Eras of Default* (chap. IV in Chatters, Municipal Debt Defaults); Report of the Securities and Exchange Commission on the Study and Investigation of the Work, Activities, Personnel and Functions of Protective and Reorganization Committees (1936), Pt. IV: Committees for the Holders of Municipal and Quasi-Municipal Obligations, *passim*; Dimock, *Legal Problems of Financially Embarrassed Municipalities*, contained in Summary of Proceedings, American Bar Assn., 1st Annual Meeting (1935), Section of Municipal Law, p. 12.

How, then, can claims against a financially embarrassed city be enforced? Experience shows that three conditions are essential if the municipality is to be kept going as a political community and, at the same time, the utmost for the benefit of the creditors is to be realized: impartial, outside control over the finances of the city; concerted action by all the creditors to avoid destructive action by individuals; and rateable distribution. In short, what is needed is a temporary scheme of public receiver-

ship over a subdivision of the state. A policy of every man for himself is destructive of the potential resources upon which rests the taxing power which in actual fact constitutes the security for unsecured obligations outstanding against a city.

To deny a state the means of giving substance to the taxing power which alone gives meaning to unsecured municipal obligations, is to hold in effect that the right to pursue a sterile litigation is an "obligation" protected by the Constitution of the United States. For there is no remedy when resort is had to "devices and contrivances" to nullify the taxing power which can be carried out only through authorized officials. See *Rees* v. *City of Watertown*, 19 Wall. 107, 124. And so we have had the spectacle of taxing officials resigning from office in order to frustrate tax levies through mandamus, and officials running on a platform of willingness to go to jail rather than to enforce a tax levy (see Raymond, State and Municipal Bonds, 342-43), and evasion of service by tax collectors, thus making impotent a court's mandate. *Yost* v. *Dallas County*, 236 U. S. 50, 57. But if taxes can only be protected by the authority of the state and the state can withdraw that authority, the authority to levy a tax is imported into an obligation to pay an unsecured municipal claim, and there is also imported the power of the state to modify the means for exercising the taxing power effectively in order to discharge such obligation, in view of conditions not contemplated when the claims arose. Impairment of an obligation means refusal to pay an honest debt; it does not mean contriving ways and means for paying it. The necessity compelled by unexpected financial conditions to modify an original arrangement for discharging a city's debt is implied in every such obligation for the very reason that thereby the obligation is discharged, not impaired.

More than fifty years ago, Lord Bryce pointed out that the debt and taxation of American cities had reached "an alarming figure". Bryce, The American Commonwealth, p. 607. Beginning with 1915, the evil consequences of the unhealthy financial conditions of New Jersey municipalities began to occupy the attention of its legislature. Investigations by expert bodies led to a series of enactments tightening state control over municipal finances. See Reports of New Jersey Legislative Commission for the Survey of Municipal Financing, 1915, 1916, 1917; Reports of New Jersey Commission on Municipal Taxation and Finance, particularly Report No. 2 (Municipal and County Debt, 1931). The depres-

sion intensified the need for state control, and the establishment of the Municipal Finance Commission with the powers outlined above were designed, as stated by the legislature, to meet "the public emergency arising from a default in the payment of municipal obligations, and the resulting impairment of public credit." But this emergency, as the decisions in this Court during the last ten years amply testify, did not evaporate. Students of the subject have pointed out that in the depression of 1893 as in that of 1873 "the worst financial difficulties for municipalities came in the fourth year of the depression". See Hillhouse, *supra,* at 14. History repeated itself, certainly as to New Jersey municipalities. See Report of New Jersey Municipal Finance Commission, 1937, and Second Annual Report of the Local Government Board (to which the functions of the Municipal Finance Commission were transferred in 1939), 1940, p. 11. The whole history of New Jersey legislation leaves no doubt that the state was bent on holding the municipalities to their obligations by utilizing the most widely approved means for making them effective. The intervention of the state in the fiscal affairs of its cities is plainly an exercise of its essential reserve power to protect the vital interests of its people by sustaining the public credit and maintaining local government. The payment of the creditors was the end to be obtained, but it could be maintained only by saving the resources of the municipality—the goose which lays its golden eggs, namely, the taxes which alone can meet the outstanding claims.

The real constitutional question is whether the Contract Clause of the Constitution bars the only proven way for assuring payment of unsecured municipal obligations. For, in the light of history, and more particularly on the basis of the recommendations of its expert advisers, the New Jersey legislature was entitled to find that in order to keep its insolvent municipalities going and at the same time fructify their languishing sources of revenue and thus avoid repudiation, fair and just arrangements by way of compositions, scrutinized and authorized by a court, might be necessary, and that to be efficacious such a composition must bind all, after 85 per cent of the creditors assent, in order to prevent unreasonable minority obstruction. As the court below pointed out, in view of the slump of the credit of the City of Asbury Park before the adoption of the plan now assailed, appellants'

bonds had little value; the new bonds issued under the plan, however, are not in default and there is a very substantial market for them. The refunding scheme, as part of an comprehensive plan for salvaging Asbury Park, both governmentally and financially, was so successful that the refunding bonds were selling at around 69 at the time of refunding, while at about the time the present suit was brought commanded a market at better than 90. See Second Annual Report of the New Jersey Local Government Board, 1940, p. 39.

From time to time, ever since *Sturges* v. *Crowinshield*, 4 Wheat. 122, 199, it has been stated that a state insolvency act is limited by the Contract Clause of the Constitution in authorizing composition of pre-existing debts. So it is, but it all depends on what is affected by such a composition and what state power it brings into play. The dictum from *Sturges* v. *Crowinshield* is one of those inaccurate generalizations that has gained momentum from uncritical repetition.

If a state retains police power with respect to building and loan associations, *Veix* v. *Sixth Ward Assn.*, 310 U. S. 32, 38, because of their relation to the financial wellbeing of the state, and if it may authorize the reorganization of an insolvent bank upon the approval of a state superintendent of banks and a court, but over the dissent of one-fourth of the depositors (except preferred or secured claimants), *Doty* v. *Love*, 295 U. S. 64, a state should certainly not be denied a like power for the maintenance of its political subdivisions and for the protection not only of their credit but of all the creditors by an adjustment assented to by at least 85 per cent of the creditors, approved by the commission of the state having oversight of its municipalities, and found wise and just after due hearing by a court.

The Constitution is "intended to preserve practical and substantial rights, not to maintain theories." *Davis* v. *Mills*, 194 U. S. 451, 457. Particularly in a case like this are we in the realm of actualities and not of abstractions and paper rights, of what things are worth in dollars and cents, and in what is proposed to realize paper values. "The question whether the remedy on this contract was impaired materially is affected not only by the precarious character of the plaintiff's right, but by considerations of fact—of what the remedy amounted to in practice." *Pittsburgh Steel Co.* v. *Baltimore Eq. Soc.*, 226 U. S. 455, 459.

This was said of the claim of a creditor of a private corporation. How much more pertinent is it to claims of these appellants against the municipality of Asbury Park in the circumstances before us.[2] To say that the right of the Asbury Park bondholders in 1935 was a precarious character is pure understatement. And we have already seen how empty was the remedy with which to enforce that right.

"In the books there is much talk about distinctions between the substance of the contract and changes of the remedy . . . . The dividing line . . . at times obscure." *Worthen Co.* v. *Kavanaugh*, 295 U. S. 56, 60. The dividing line will remain obscure if we deal with empty abstract rights instead of worldly gains and losses, if we indulge in doctrinaire talk about "rights" and "remedies", instead of giving these concepts a content that carries meaning to the understanding of men. Here we have no such action as that disclosed in *Worthen Co.* v. *Kavanaugh*, *supra*, where with "studied indifference to the interest of the mortagee or to his appropriate protection", legislation was found "to have taken from the mortgage the quality of an acceptable investment for a rational investor," and the challenged changes of remedy were found to be "an oppressive and unnecessary destruction of nearly all the incidents that give attractiveness and value to collateral security". Here we have just the opposite—no security whatever except the effective taxing power of the municipality; the effective taxing power of the municipality prostrate without state intervention to revive the famished finances of the city; state intervention, carefully devised, worked out with scrupulous detail and with due regard to the interests of all the creditors.

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[2] Compare Chicago &c. Railroad *v.* Nebraska, 170 U. S. 57, 72. "Usually, where a contract, not contrary to public policy, has been entered into between parties competent to contract, it is not within the power of either party to withdraw from its terms without the consent of the other; and the obligation of such a contract is constitutionally protected from hostile legislation. Where, however, the respective parties are not private persons, dealing with matters and things in which the public has no concern, but are persons or corporations whose rights and powers were created for public purposes, by legislative acts, and where the subject-matter of the contract is one which affects the safety and welfare of the public, other principles apply. Contracts of the latter description are held to be within the supervising power and control of the legislature when exercised to protect the public safety, health and morals, and that clause of the Federal Constitution which protects contracts from legislative action cannot in every case be successfully invoked. The presumption is that when such contracts are entered into it is with the knowledge that parties cannot, by making agreements on subjects involving the rights of the public, withdraw such subjects from the police power of the legislature."

and scrutinized to that end by the state judiciary with the result that that which was a most depreciated claim of little value has, by the very scheme complained of, been saved and transmuted into substantial value. To call a law so beneficent in its consequences on behalf of the creditor who, having had so much restored to him, now insists on standing on the paper rights that were merely paper before this resuscitating scheme, an impairment of the obligation of contract is indeed to make of the Constitution a code of lifeless forms instead of an enduring framework of government for a dynamic society.

We do not go beyond the case before us. Different considerations may come into play in different situations. Thus we are not here concerned with legislative changes touching secured claims. The New Jersey courts have held that under this very statute tax anticipations and revenue notes stand on an entirely different footing from other municipal obligations and in relation to them no claim is affected by the Municipal Finance Commission Act of 1931. *State* v. *Fort Lee*, 14 N. J. Misc. 895. The differentiation thus made by New Jersey regarding various obligations in itself indicates the detailed care with which the legislation of the State proceeded in readjusting outstanding municipal obligations.

Affirmed.

Mr. Justice REED concurs in the result.

A true copy.

Test:

Clerk, Supreme Court, U. S.